Department of Foreign Affairs
and International Trade

Ministère des Affaires étrangères
et du Commerce international

CANADA

RECENT TRENDS IN FOREIGN DIRECT INVESTMENT:

A COMPARISON OF CANADA WITH THE USA AND MEXICO

Nipa Banerjee

The Trade and Economic Analysis Division (EET)
Department of Foreign Affairs and International Trade

December 1997

Reference Document No. 2

Department of Foreign Affairs
and International Trade

REFERENCE DOCUMENT NO. 2

RECENT TRENDS IN FOREIGN DIRECT INVESTMENT:

A COMPARISON OF CANADA WITH THE USA AND MEXICO

by

Nipa Banerjee

December 1997

Executive Summary

The objective of this study is to provide a non-technical descriptive review of inward Foreign Direct Investment (FDI) data with respect to Canada, the US, and Mexico. The paper provides an overview of FDI trends over the 1985-94 period and then addresses two related issues. First, what role does FDI play in a country's economy, and what specifically is its role in Canada? Second, data is presented on FDI trends in the North American region during the study period.

In regard to the linkage between FDI and the Canadian economy, a number of observations are made. Importantly, the data confirms that the share of FDI stock in Canada's GDP, and its gross fixed capital formation, is significant. The complementarity between trade and FDI is also strong in the Canadian case. Foreign companies' share of the total revenues generated by all businesses in Canada been increasing, and foreign affiliates' share in Canadian trade is high. The export and import propensities of the Canadian subsidiaries or affiliates of foreign investors are also high.

A comparison of FDI data reveals no significant increase in the share of FDI in Canada's GDP between the 1980's and 1990's. Throughout the study period, the role of FDI in gross capital formation is significant in Canada, the US, and Mexico. For Canada a comparison of the figures in the mid-1980's and 1990's, in both areas (FDI's share in GDP and in gross capital formation), does not suggest significant differences.

The data on FDI trends in the North American region during the study period was the second issue addressed in this paper. The total quantity of FDI increased in Canada, the US, and Mexico over the period. The Canadian share of annual global FDI inflow during the latter period, however, was lower than the earlier period. In terms of the US FDI to Canada, the US share has declined since 1985, but has begun to increase during the 1990s.

The data further indicate that the share of Canadian FDI stocks in the US appears to have increased slightly since 1989. Moreover, 1995 data on FDI flows indicates that Canada's share in the US increased significantly. What is clear from the data presented in the paper is that despite the increase in the total volume of FDI in Canada, its share of global FDI has declined.

I. Introduction

The objective of this paper is to provide an overview of inward Foreign Direct Investment (FDI) in Canada, the US and Mexico over the 1985-1994 period. The analysis has been undertaken to highlight trends in inward FDI. The paper addresses two key issues. First, it considers the theoretical role FDI plays in a country's economy. Secondly, data is presented on FDI trends in the North American region over the study period.

The next section briefly reviews the theoretical aspects of trade and FDI linkages, and the impact of FDI on a country's economy. Section III discusses the role of FDI in the Canadian economy. Section IV presents data on FDI in Canada, the US and Mexico. Section V summarizes the paper.[1]

II. Trade and FDI Linkages

It is widely recognized that FDI can have a range of effects, such as employment creation[2], physical capital formation[3] and domestic investment[4], human capital development[5], transfer of technology[6] and increased productivity[7] (especially in the manufacturing sector)[8] and finally, economic growth[9]. Trade and FDI are also interrelated activities. Two sets of links are highlighted in the literature. The first is the impact of trade policies on FDI. The pattern of trade and trade policies may influence the size, direction and composition of the FDI flows[10]. Trade policies, such as tariff barriers, can for example serve as incentives to FDI inflows, either

---

[1]The definitions of Foreign Direct Investment (FDI) and related terms are provided in Annex 1.

[2]WTO (1996); Messerlin (1996); McCulloch in Froot (1993); McCharles (1985); Mohnen (1992); Baldwin (1995); Schwanen (1997).

[3]UNCTAD (1996).

[4]WTO (1996).

[5]Lipsey, Blomstrom & Kravis (1990); Messerlin (1995); WTO (1996).

[6]Aitkin, Hanson & Harrison (1994); Lipsey, Blomstrom & Kravis (1990); Mansfield & Romeo (1980); Findley in *Quarterly Journal of Economics* (1978).

[7]Blomstrom (1986); Blomstrom & Wolff (1994); Caves (1974).

[8]Graham (1996).

[9]Globerman (1979); Blomstrom, Lipsey & Zejan (1992).

[10]McCulloch in Froot (1993); Fujimora (1994).

as a deliberate act of policy or inadvertently[11]. An interest in jumping a high tariff, for instance, can induce foreign direct investment in the local market. Other import barriers, such as quantitative limits on imports in a particular sector, could also induce FDI in the form of expanded production in the local market[12]. Regional (or in some cases global) trade agreements and economic integration may also influence FDI decisions by firms.[13] Larger market size, resulting from regional trade agreements, provide opportunities for investors to take advantage of economies of scale and, therefore, encourage investment flows.[14] Rules of Origin, which distinguish between products produced by countries party to the regional agreement and those that are not, also may induce third country investment.[15]

The second set of links is the impact of FDI on trade.[16] FDI policies by affecting investment decisions, influence the size, direction and composition of trade[17] and subsequently its contribution to growth and development[18]. FDI can have sweeping and dynamic effects on the host country as it stimulates capital formation, competition, innovation, productivity[19] and savings. All these factors can impact on a country's import and export activities. Several

---

[11]McCulloch in Froot (1993).

[12]Bhagwati (1985); Bloningen & Feenstra (1996).

[13]The possibility not only of increased intra-regional investment, but also of increased third country investment were powerful incentives for Canada to take part in developing and agreeing to the investment provisions of the FTA and NAFTA.

[14]Rugman (1990). It has been observed that in regional trade areas, e.g., in the European Union, investment flows between the member and non-member third countries have increased substantially: UNCTAD (1993); WTO (1995).

[15]Hindley (1990); Kruegar (1995). Normally, members of free trade agreements maintain their own external tariff schedules. This creates the need for "rules of origin" to determine if inputs originating in a non-member country and imported into the free trade zone by a member country for further processing would receive free trade treatment when the final product is exported to another member country. Rules of origin can have a protectionist effect and lead a member investor to source inputs inside the free trade area. This would encourage non-member countries to invest within the free trade area. Similarly, the Hub and Spoke system may influence investment choices, with investors preferring to invest in the "hub" than the "spoke". Baldwin (1993) WTO (1995).

[16]Only the impact of FDI on host country's exports and imports is discussed in the paper because of the focus on inward FDI stocks and flows.

[17]McCulloch in Froot (1993); OECD (1993); Fujimora (1994).

[18]UNCTAD (1997).

[19]Caves (1974).

studies, covering a number of sectors, confirm a positive relationship between FDI inflows in the host country and the total volume of a host country's exports[20].

Moreover, there is some evidence to suggest that in general, foreign-owned firms have a higher propensity to export than locally-owned firms. Foreign firms often have a better knowledge of the international market and can more quickly respond to changing international demands[21]. The size and efficiency of their distribution network may also give foreign firms an advantage[22]. Several studies also show that foreign affiliates can have a positive spill-over impact on the export propensity of local firms[23]. Export performance may also be encouraged through FDI policy. Investment policies, such as those seeking to impose a mandatory requirement to export a certain portion of the local production[24] and/or FDI policy biased towards export-oriented sectors, are designed with export promotion in mind[25].

The evidence on the relationship between FDI and imports is mixed. Some studies indicate that the inflow of FDI reduces host country's imports[26]. Other studies find that inward FDI raises host country's import levels[27]. Affiliates normally have a high propensity to import intermediate inputs from the home country, particularly when such inputs are either not available in the host country or the quality of the local supplies is not assured[28].

---

[20]World Bank (1997); Hill (1990); Lipsey (1991).

[21]Chen (1994).

[22] The role played by intra-corporate or intra-firm trade is significant in North America.

[23]Hill (1990); Aitken, Hansen & Harrison (1994).

[24]The WTO TRIMS (Trade Related Investment Measures) are inconsistent with these types of restrictions. See the Chapter on TRIMS (the Illustrative List in the Annex) in *The Results of the Uruguay Round of Multilateral Trade Negotiations Legal Texts* (1994).

[25]For instance, the deliberate policies of host governments to set up export promotion zones (e.g., the Free Economic Zones in East Asia) to stimulate export, employment, and technology transfer have encouraged foreign firms to establish affiliate operations in these zones. Graham & Krugman (1993); Graham & Anzai (1994); Naujoks & Scmidt (1995).

[26]WTO (1996).

[27]Graham & Krugman (1993); Graham & Anzai (1994); Naujoks & Schmidt (1995).

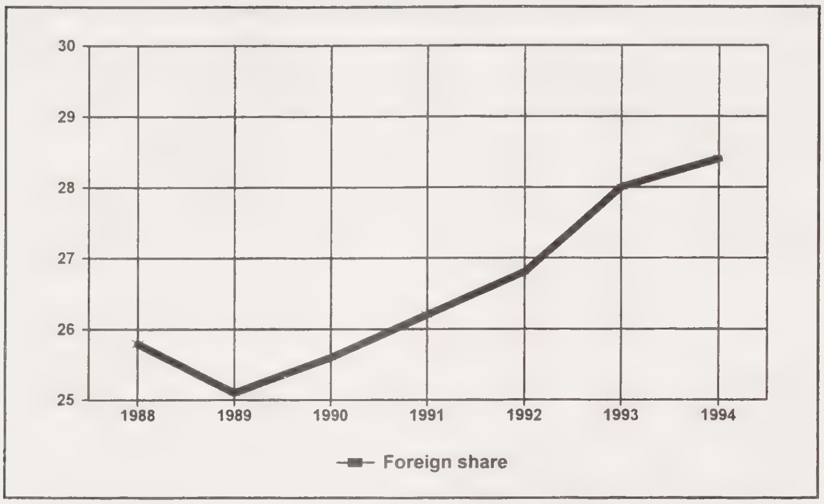
[28]OECD (1993).

III. The Role of FDI in Canada's Trade and Economy

There is a fair amount of empirical evidence that FDI and the foreign affiliates play an important role in Canada's economy. A study by Industry Canada illustrates that the importance of foreign firms, as measured by their share of the total revenues generated by all businesses operating in Canada, has been on the rise throughout the 1990s[29]. Chart I shows the rise in market share of the foreign affiliates in Canada. Of note, starting in 1989, is the fact that foreign shares of revenue generated in Canada has increased significantly.

Chart I

Foreign Shares of the Revenues Generated by Businesses in Canada



Source: Cameron, Industry Canada Study, 1997

Tables I and II present data on the role played by FDI in Canada, the US, and Mexico as reflected by the proportion of FDI in these countries' gross domestic product, and gross capital formation.

[29] Cameron (1997).

Table I

Share of FDI Stock in GDP
Canada, the USA & Mexico 1980,1985,1990,1994 & 1995
(Percentage)

Year	Canada	USA	Mexico
1980	20.4	3.1	4.6
1985	18.4	4.6	10.5
1990	19.7	7.2	13.3
1994	19.2	7.5	14.4
1995	20.6	7.8	24.5

Source: UN, World Investment Report 1996

Table I illustrates that for Canada, the share of FDI stock in the GDP is significantly higher than in the USA. Up to 1994, the share of FDI in Canada's GDP was lower than the 1980 figure. The share then increased in 1995 to slightly more than the 1980 level. Overall, no strong trend in the direction (increase or decrease) in FDI's share in Canada's GDP can be identified in the period. Mexico and the US show different trends, since 1980, the share of FDI stocks in the US's and in Mexico's GDP has increased. Mexico in particular experienced a sharp increase in the share of FDI stock in GDP. The 1995 figure for Mexico shows a significant increase, which partly reflects a real decline in its GDP that year.

Table II

Share of FDI Inflow in Gross Fixed Capital Formation
Canada, the USA and Mexico 1984-1995
(percentage)

Year	*Canada*	*USA*	*Mexico*
1984-89 (annual average)	*5.4*	*5.8*	*7.8*
1990	*6.5*	*6.0*	*5.6*
1991	*2.4*	*3.0*	*8.5*
1992	*4.2*	*2.2*	*6.4*
1993	*5.0*	*4.7*	*6.0*
1994	*5.9*	*4.8*	*10.4*
1995	*11.4*	*4.83*	*17.14*

Source: UNCTAD, World Investment Report 1996

Table II presents the share of FDI in gross capital formation of Canada, the US, and Mexico. In all three countries, FDI plays a role in gross capital formation. FDI is most significant for Mexico, followed by Canada and then the US. In 1995, the increase in the share of FDI in gross capital formation was particularly marked for both Canada and Mexico. Whether or not this indicates the beginning of a trend, at least with respect to Canada, can only be determined when further data become available.

An important question for Canada is whether FDI is trade enhancing or trade substituting. The data on percentage proportions of intra-firm trade in total Canada-US trade suggests that FDI is a trade enhancing factor. A recent study by Investment Canada shows that the foreign owned manufacturing affiliates in Canada display higher import and export propensities and are more outward-oriented than their domestic counterparts[30]. The conclusion of the study was that intra-firm trade (for which FDI is a precondition) plays a significant role in Canada's economic development.

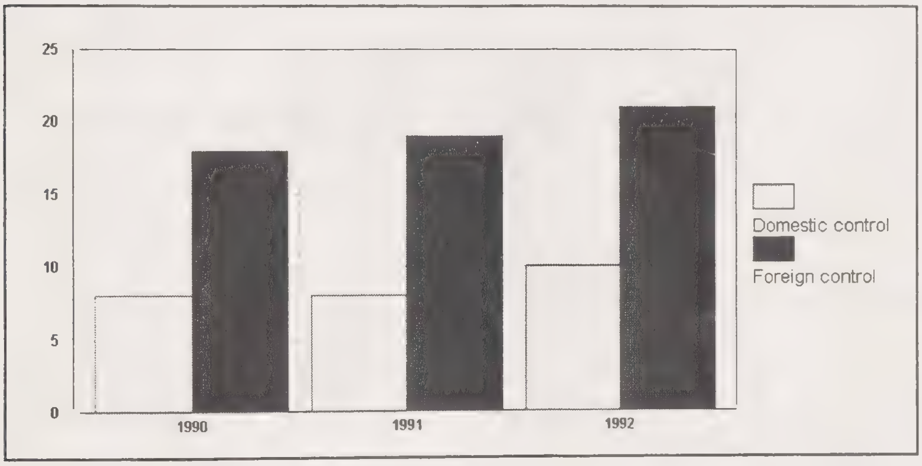
Charts II, III and IV confirm the complementary role that trade and FDI play in Canada. Charts II and III in particular show the degree of export and import orientation of foreign versus the domestic firms. They indicate that foreign firms in Canada are more export-oriented and

[30]Covari and Wisner (1993).

import-oriented than domestic firms[31]. A recent study by Industry Canada found that the export orientation of the foreign firms is more than twice that of the domestic firms over the 1990-92 period while their import orientation is three times more than that of the domestic firms over the same period[32]. The study found that foreign affiliates in Canada accounted for 44% of the total exports over 1990-92; total imports of foreign affiliates in Canada amounted to 51.1% of the total goods imported into Canada over 1990-92.

Chart II

The Degree of Export Orientation : Foreign vs Domestic Firms



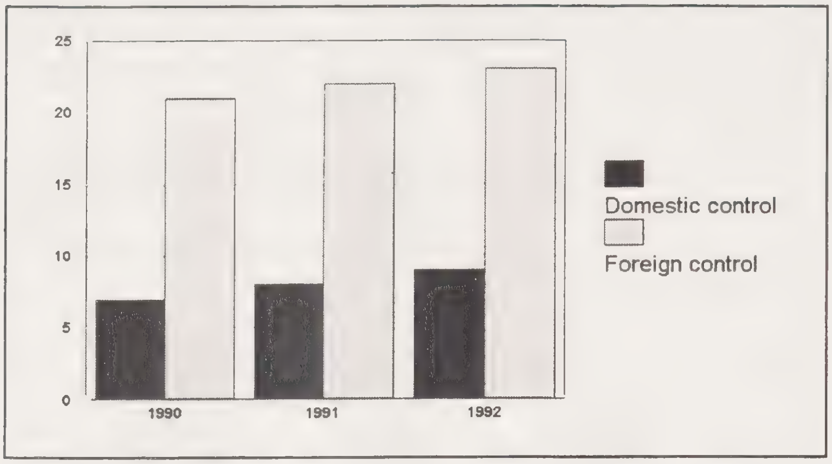
Source: Cameron, Industry Canada Paper, 1997

[31]The export and import orientations are measured by the proportion of exports and imports in the total sale of the firms: Cameron (1997).

[32]Ibid.

Chart III

The Degree of Import Orientation : Foreign vs Domestic Firms



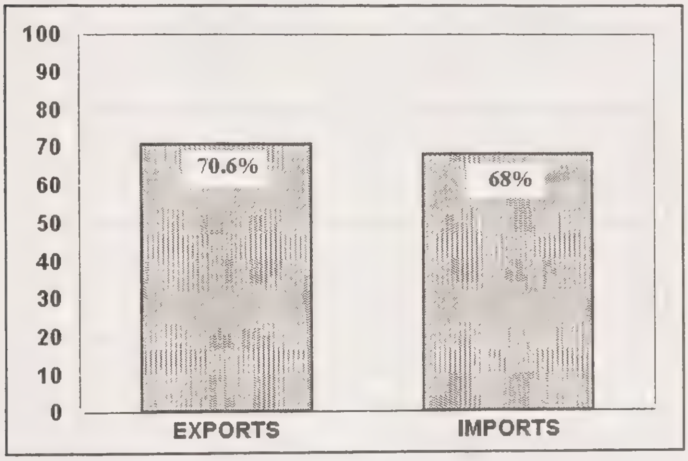
Source: Cameron, Industry Canada Paper, 1997

Chart IV reflects the export and import propensities of US affiliates in Canada and underscores the importance of FDI for Canadian trade. Chart IV, Figure 1, demonstrates that 70% of total exports of US affiliates in Canada are intra-firm, while 68% of their imports are intra-firm. Overall, the data presented in this section indicate that FDI plays an important role in Canada's economy, as judged by the proportion of FDI in Canada's GDP, gross capital formation, and trade.

Chart IV

Intra-Firm Trade of US Affiliates in Canada
Position in 1992 (in percent)

Figure 1: As a Proportion of Total Trade of US Affiliates in Canada



Source: Cameron, Industry Canada Paper, 1997

Figure 2: As a Proportion of Total Canada-US Trade

Source: Cameron, Industry Canada Paper, 1997

IV. Trends in FDI

This section addresses the central question of what the Canadian FDI experience is over the period of study?[33] For the purpose of identifying FDI trends within the region, aggregated data is presented for two periods: 1985 to 1989; and (ii) 1990 to 1994. The data provides the basis for comparing the FDI trends in the two periods[34].

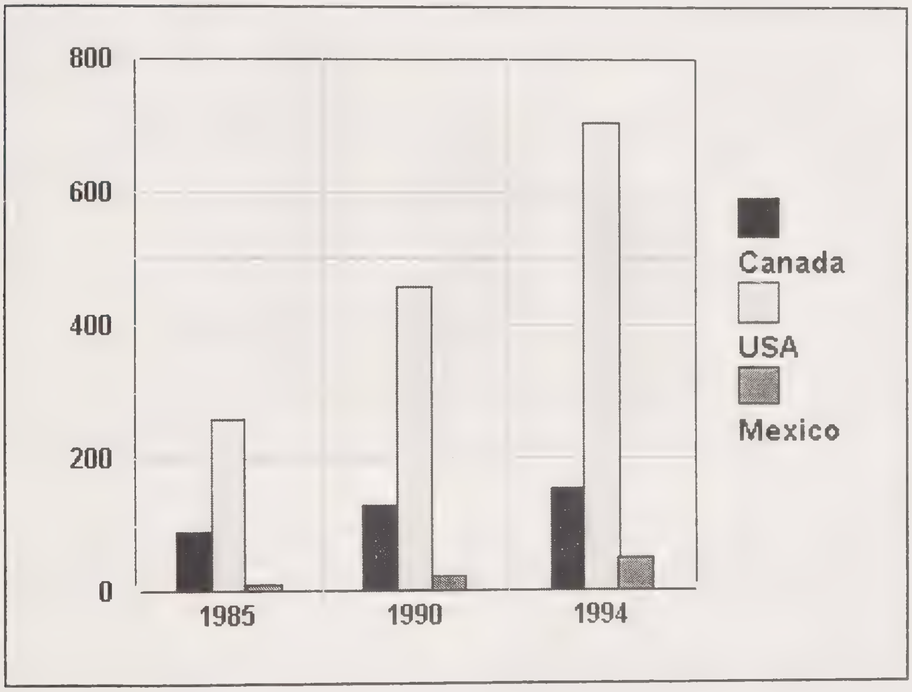
Charts V and VI and Tables III to VI present data on FDI stocks. Chart V traces the FDI stock position (in current Canadian billion dollars) of the three NAFTA signatories through 1985, 1990 and 1994. The Chart shows that in all three countries, total FDI stocks increased, with the highest value, not unexpectedly, recorded for the US in all the years surveyed. Chart VI presents some more recent data for Canada.

[33]For assessments of NAFTA, which cover most of this period, see Rugman & Verbeke, Rugman & Gestrin, Nymark & Verdun and Globerman; all in Rugman ed. *Foreign Investment & NAFTA* (1994); Rugman & Gestrin in *Commentary* (1993).

[34]Consistent data on FDI stocks and flows is available for the FTA/NAFTA signatory countries up to 1994. Therefore, the data analysis is done for the post FTA/NAFTA period up to 1994 only.

Chart V

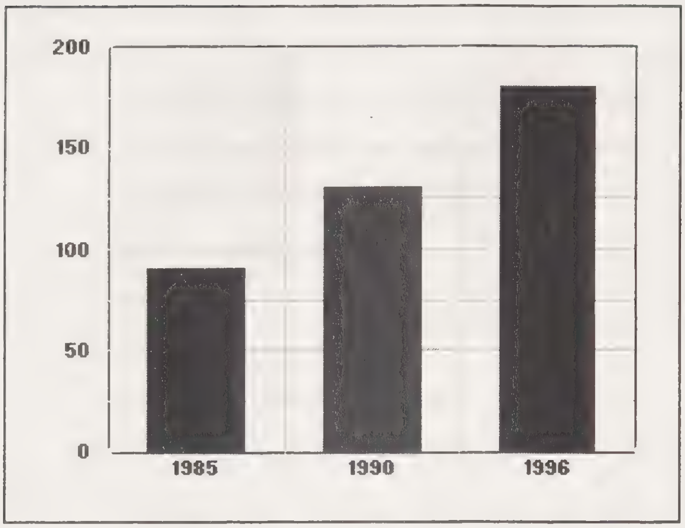
Stock of FDI in Canada, the USA and Mexico 1985, 1990 and 1994
(In current C$ billion)



Source: Statistics Canada, Canada's Investment Position, Catalogue No. 67-202-XPB

Chart VI

Stock of FDI in Canada 1985-1996
(in current C$ billion)



Source: *Statistics Canada,* *Canada's Investment Position 1926-1996*, *Catalogue No. 67-202-XPB, 1997*

Nonetheless, the total dollar value of FDI stocks provides only a partial picture of the trend and changes. Tables III, IV, and V present data on the shares of FDI stocks in Canada, the US, and Mexico by country of origin or source for 1985, 1989, and 1994. The data shows how the FDI shares changed over the study timeframe, including how the shares of the and the pattern of stock shares of the three countries have changed.

The Table III data shows that the US's share in Canadian FDI stock is the largest, although a decline in the percentage held by the US is visible since 1985. Conversely, Japanese and other countries' shares have increased since 1985.

Table III

Share in Canadian FDI Stock by Source (Country of Origin)
1985, 1989 and 1994 (in percent)

Source Country or Region	*1985*	*1989*	*1994*
EU	*17.1*	*22.6*	*20.7*
USA	*75.1*	*65.7*	*66.4*
Japan	*2.5*	*3.9*	*4.3*
Mexico	*0.01*	*0.01*	*0.12*
Other Countries	*5.3*	*7.8*	*8.4*
Total	*100.0*	*100.0*	*100.0*

Source: Based on data from OECD, International Direct Investment Statistics Yearbook

Table IV provides the FDI stock figures in the US up to 1994. The EU has dominated US FDI stocks although its share has declined since 1985. In 1995, the joint share of UK and other European countries was 64.41%.[35] Since 1985, Japan's share of FDI has doubled (although Japan's share at 19.39% decreased a little in 1995). Japan's share has also increased in Mexico (to 4.5%) and Canada (to 4.3%). Of note, in 1995, is the fact that Canada's share of investment flow into the US increased significantly, accounting for roughly 11% of the total.

---

[35]The 1995 figures for FDI stocks in the US is based on the data provided in *Survey of Current Business, Vol. 77, No.6, June 1997,* US Department of Commerce, Economics & Statistics Administration, Bureau of Economic Analysis, 1997.

Table IV

Share in US FDI Stock by Source (country of origin)
1985,1989 and 1994 (in percent)

Source Country or region	1985	1989	1994
EU	57.9	57.6	53.9
Canada	9.3	8.2	8.4
Japan	10.5	18.2	22.9
Mexico	0.3	0.1	0.5
Other Countries	22.1	15.9	14.4
Total	100.0	100.0	100.0

Source: Based on data from OECD, International Direct Investment Statistics Yearbook 1996 & 1997

The US share dominates in Mexico although a decline in the share from the mid-1980's is clear from the table. The Canadian share has not undergone any significant change.

Table V

Share in Mexican FDI Stock by Source (country of origin)
1985, 1989, and 1994 (in percent)

Source Country or Region	1985	1989	1994
EU	16.2	22.9	21.8
USA	69.8	58.6	52.3
Japan	3.2	3.3	4.5
Canada	2.3	1.8	2.0
Other Countries	8.5	13.3	19.4
Total	100.0	100.0	100.0

Source: Based on data from OECD, International Direct Investment Statistics Yearbook 1996

Table VI presents comparative data on FDI flows as a percentage of global flows to Canada, the US, and Mexico. The figures reflect the fact that FDI inflow shares are volatile, with substantial changes from year-to-year. Reflecting the size of its economy, the US's share of global FDI flow is significantly higher than those of both Canada and Mexico. The Mexican share of global investment inflows, at least since 1991, is almost as high as that of Canada. Notably, both US and Canadian shares in global FDI inflow have declined since the 1984-89 period.

Although Table VI shows a decline in Canadian and US shares in global FDI flows, this says nothing of the total dollar value of the investment flow into these countries. For the three countries, the total value of FDI inflows increased over the period under survey. This is explained by the fact that the total value of global flows has been increasing very quickly, faster than in North America.

Table VI

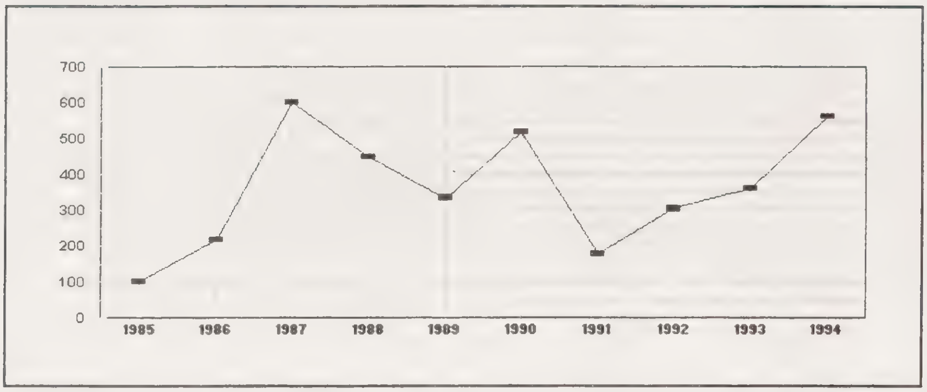
Shares in World FDI Inflow :Canada, US and Mexico
Annual Breakdown 1984-1995 (in percent)

Year	*Canada*	*USA*	*Mexico*
1984-89 Annual Average	*4.1*	*38.1*	*2.1*
1990	*3.9*	*23.5*	*1.3*
1991	*1.7*	*14.0*	*3.0*
1992	*2.7*	*10.5*	*2.6*
1993	*2.4*	*19.8*	*2.1*
1994	*2.7*	*22.1*	*3.5*
1995	*3.6*	*19.1*	*2.2*

Source: UNCTAD, World Investment Report 1996

Chart VII

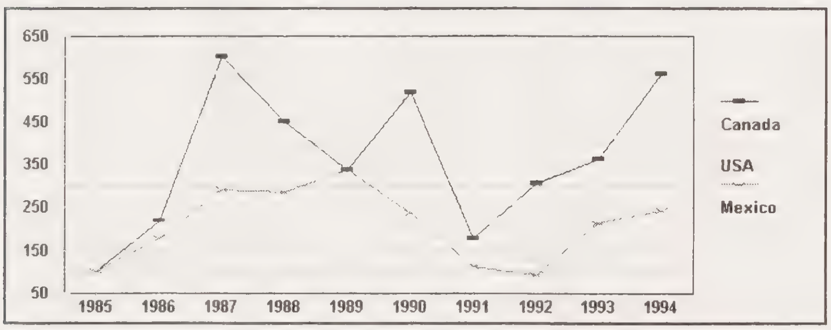
Index of FDI Inflows : Canada
(Index 1985=100)



Source: OECD International Direct Investment Statistcs Year Book, 1996

Chart VIII

Index FDI Inflow:Canada, Mexico and the USA
(Index 1985=100)



Source: OECD International Direct Investment Statistics Year Book 1996

Chart VII shows the flow of FDI into Canada from 1985 to 1994. FDI inflows to Canada have had a series of ups and downs, with the trend after 1991 showing a continuous increase.

Chart VIII also gives a comparative look into the FDI inflow pattern of the three NAFTA partners, and illustrates that Canada has the most variability over the study period.

V. Conclusion

The objective of this study has been to provide a non-technical descriptive interpretation of inward FDI data in respect to Canada, the US, and Mexico over the past decade. In regard to the linkage between FDI and the Canadian economy, a number of observations can be made. Importantly, the data confirms that the share of FDI stock in Canada's GDP, and its gross fixed capital formation, is significant. The complementarity between trade and FDI is also strong in the Canadian case. Foreign companies' share of the total revenues generated by all businesses in Canada has been increasing, and foreign affiliates' share in Canadian trade is high. The export and import propensities of the Canadian subsidiaries or affiliates of foreign investors is also high.

A comparison of FDI data reveals no significant increase in the share of FDI in Canada's GDP since 1989. Throughout the study period, the role of FDI in gross capital formation is significant for Canada, the US, and Mexico. For Canada, in both areas (FDI's share in GDP and in gross capital formation), a comparison of the figures in the mid-1980's and 1990's does not suggest significant differences.

The data on FDI trends in the North American region during the study period is the second issue addressed in the paper. The total quantity of FDI increased in Canada, the US, and Mexico over the study period. The Canadian share of annual global FDI inflow during the latter period was lower than the earlier period. In terms of the US FDI to Canada, the US share has declined since 1985, but has begun to increase during the 1990s.

The data further indicate that the share of Canadian FDI stocks in the US appears to have increased slightly since 1989. Moreover, 1995 data on FDI flows indicates that Canada's share in the US increased significantly. What is clear from the data presented is that despite the increase in the total volume of FDI in Canada, its share of global FDI has declined in recent years.

REFERENCES AND BIBLIOGRAPHY

Ahsan S. M., and Wang T. "Canadian Foreign Direct Investment in Asia", unpublished paper, Concordia University, 1997.

Aitken B., Hanson G., and Harrison A. "Spill-Overs, Foreign Investment and Export Behaviour", *NBER Working Paper No. 4967*, December 1994.

Baldwin R. "Adapting the GATT to a More Regionalized World: A Political Economy Perspective", in Anderson K. and Blackhurst R. *Regional Integration and the Global Trading System*, Harvester Wheatsheaf, 1993.

Baldwin R. "The Effect of Trade and Foreign Direct Investment on Employment and Relative Wages", *NBER Working Paper No. 5037*, February 1995.

Bhagwati J. "VERs, Quid Pro Quo DFI and VIEs; Political Economy Theoretic Analysis", *International Economic Journal Vol. 1 No. 1*, Spring 1987.

Blomstrom M., Lipsey R., and Zejan M., "What Explains Developing Country Growth", in *NBER Working Paper No. 4132*, 1992.

Blomstrom M. "Foreign Investment and Productive Efficiency: The Case of Mexico", in *The Journal of Industrial Economics, 35*, 1986.

Blomstrom M., Kokko A. and Zejan M. "Host Country Competition and Technology Transfer by Multinationals", *NBER Working Paper No. 4131*, August 1992.

Blomstrom M., and Wolff E. "Multinational Corporations and Productivity Convergence in Mexico", *NBER Working Paper No. 1923*, 1994.

Blonigen B., and Feenstra R. "Protectionist Threats and Foreign Direct Investment", *NBER Working Paper 5475*, 1996.

Cameron R. "Trade Activity of Foreign Affiliates in Canada, Unpublished *Industry Canada Paper*, 1997.

Caves R. "Multinational Firms, Competition & Productivity in Host Country Markets", *Economica Vol. 41 No. 162*, 1974.

Chand R. "NAFTA: The Economic Implications for Canada", *The Conference Board of Canada, International Business Research Centre*, 1993.

Chen E. "Transnational Corporations and Technology Transfer to Developing Countries", *Routledge for the UN*, London, 1994.

Covari R., and Wisner R. "Foreign Multinationals and Canada's International Competitiveness", *Investment Canada Working Paper No. 16*, June 1993.

Culem C. G. "The Locational Determinants of Direct Investments Among Industrialized Countries", *European Economic Review 32*, 1988.

Department of Foreign Affairs and International Trade, Government of Canada. "NAFTA Update: A Selected Bibliography", Library, DFAIT, 1997.

Economic Council of Canada. "Managing Adjustment", 1988.

Ethier W. "The Multinational Firm", *The Quarterly Journal of Economics,* John Wiley & Sons, Cambridge, 1986.

Findley R. "Relative Backwardness, Direct Foreign Investment and the Transfer of Technology: A Simple Dynamic Model", *Quarterly Journal of Economics, 92*, February, 1978.

Fry E., and Radebaugh L. eds. "Investment in the North American Free Trade Area: Opportunities and Challenges", Brigham Young University, Utah, 1992.

Fujimora J. "Global Strategies and Foreign Direct Investment: Implications for Trade and Canadian Economy", *Policy Paper*, Department of Foreign Affairs and International Trade, March 1994.

GATT. "The Results of the Uruguay Round of Multilateral Trade Negotiations: The Legal Texts", The Gatt Secretariat, Geneva, 1994.

Glickman N., and Woodward D. "The New Competitors: How Foreign Investors Are Changing the Face of the US Economy", Basic Books, New York, 1989.

Globerman S. "The Economics of NAFTA", in Rugman A. ed. *NAFTA & Foreign Investment*, South Carolina Press, Columbia, 1994.

Globerman S. "Foreign Acquisitions of Canadian High Technology Firms", in *Foreign Investment, Technology and Economic Growth,* University of Calgary Press, Calgary, 1991.

Globerman S., and Walker M. "Assessing NAFTA: A Trinational Analysis", Fraser Institute, Vancouver, 1993.

Graham E., and Krugman P. "The Surge in Foreign Direct Investment in the 1980s", in Froot K. ed. *Foreign Direct Investment,* University of Chicago Press, Chicago, 1993.

Graham E. "On the Relationship Among Direct Investment and International Trade in the Manufacturing Sector: Empirical Results for United States & Japan", Unpublished Paper, 1996.

Graham E.,and Anzai N. "The Myth of a Defacto Asian Bloc: Japan's Foreign Direct Investment in East Asia", *The Columbia Journal of World Business, 24*, 1994.

Graham E. and Krugman P. "Foreign Direct Investment in the US", Institute for International Economics, Washington, 1991.

Harris R. "The Economic Impact on Canada of Changing Trade Barriers between Canada and the US", *International Economics Working Paper DP87-6*, University of Toronto, 1987.

Hill H. "Foreign Direct Investment and East Asian Economic Development", *Asian Pacific Economic Literature, 4*, 1990.

Hindley B. "Foreign Direct Investment: The Effects of Rules of Origin", *Discussion Paper No. 30*, Royal Institute of International Affairs, London, 1990.

Hufbauer G., Lakdawalla D., and Malani A. "Determinants of Foreign Direct Investment and its Connection to Trade" *UNCTAD Review* 1994.

Krueger A. "Free Trade Agreements versus Customs Unions", *NBER Working Paper No.5084*, 1995.

Lim, L. and Pang E. "Vertical Linkages and Multinational Enterprises in Developing Countries", *World Development 10*, 1982.

Lipsey R., and Weiss M. "Foreign Production and Exports of Individual Firms" *Review of Economics and Statistics, 66,* May 1984.

Lipsey R. "Foreign Direct Investment in the United States and US Trade", *Annals of the American Academy of Political & Social Science 516*, July 1991.

Lipsey R., Blomstrom M. and Kravis I. "R&D by Multinational Firms & Host country Exports", in Evenson R. and Ramis G. eds. *Science & Technology Policy: Lessons for Developing Asia*, Westview Press, Boulder, 1990.

MacCharles D. "Trade, Investment & Knowledge Flows in Relation to the Multinational Enterprises", Institute of Research on Public Policy, Ottawa, 1985.

Mohnen P. "The Relationship between R&D and Productivity Growth in Canada and Other Industrialized countries", Economic Council of Canada, Ottawa, 1992.

Mansfield E. & Romeo A. "Technology Transfer to Overseas Subsidiaries by US Based Firms", *Quarterly Journal of Economics 95*, December, 1980.

Mansfield E. "Technology transfer, Productivity & Economic Policy", W.W. Norton, New York, 1982.

McCulloch R. "New Perspectives on Foreign Direct Investment", in Froot K.A. ed. *Foreign Direct Investment,* University of Chicago Press, Chicago, 1993.

Messerlin P. "The Impacts of Trade & Capital Movements on Labour: Evidence on the French Case", *OECD Economic Studies No. 1*, OECD, Paris, 1995.

Naujoks P. and Schmidt K. "Foreign Direct Investment and Trade in Transition Countries: Tracing Links", a Sequel, *Kiel Institute of World Economics Working Paper No. 704*, 1995.

Nymark A., and Verdun E. "Canadian Investment & NAFTA", in Rugman A. ed. *Foreign Investment & NAFTA*, University of South Carolina, Columbia, 1994.

OECD. "The Impact of Foreign Investment on Economies of OECD Countries", Paris, November 1993.

OECD. "International Direct Investment Statistics Year Book", 1996.

Prestowitz C. "Trading Places: How We Allowed the Japanese to Take the Lead", Basic Books, New York, 1988.

Rouslang D. "Comment on Frank-Freeman Paper", in Dewald W. ed. *Impact of International Trade and Investment on Employment,* Bureau of International Labour Affairs, Washington, 1978.

Rugman A. and Verbeke Alain. Foreign Direct Investment and NAFTA: A Conceptual Framework in Rugman A. ed. *Foreign Investment and NAFTA*, 1994.

Rugman A. & Gestrin M. "NAFTA's Treatment of Foreign Investment", in Rugman A ed. *Foreign Investment and NAFTA*, University of South Carolina, Columbia, 1994.

Rugman A. "Multinationals and Canada-United States Free Trade", University of South Carolina, Columbia, 1990.

Rugman A. & Gestrin M. "The NAFTA's Impact on the North American Investment Regime", *Commentary, No. 42*, C.D. Howe Institute, Toronto, 1993.

Safarian A. "Direct Investment Strategy and Canada-US Free Trade Agreement", in Reynolds C. ed. *The Dynamics of North American Trade & Investment*, Stanford University Press, Palo Alto, 1991.

Safarian A. "Free Trade & Foreign Direct Investment: Interim Report", Fry E. and Radebaugh L. eds. *Investment in the North American Free Trade Area: Opportunities and Challenges*, Brigham Young University, Utah, 1992.

Safarian A. "Canada-US Free Trade Agreement and Foreign Direct Investment", Comments to the Standing Committee on Finance & Economic Affairs, Legislature of Ontario, January 1988.

Sauve P. and Schwanen D. eds. "Investment Rules for the Global Economy", C.D. Howe Institute, Toronto, 1996.

Schwanen D. "Investment and the Global Economy: Key Issues in Rule-Making", in Sauve P. and Schwanen D. eds. *Investment Rules for the Global Economy*, 1996.

Schwanen D. "Trading Up: The Impact of Increased Continental Integration on Trade, Investment and Jobs in Canada", *Commentary No.89*, C.D. Howe Institute, Toronto, 1997.

Statistics Canada. "Canada's International Investment Position", *Catalogue No. 67-202-XPB*, 1997.

Tolchin M and Tolchin S. "Buying into America: How Foreign Money is Changing the Face of Our Nation", Times Books, New York, 1988.

UNCTAD. "World Investment Reports, 1993, 1994, 1995 & 1996", UN, New York and Geneva.

US Department of Commerce, Economics & Statistics Administration Bureau of Economic Analysis. *Survey of Current Business, Vol 77, No. 6*, June 1997.

Wigle R. "Between a Rock and a Hard Place: The Economics of Canada-US Free Trade", *Canadian Public Policy 14*, 1988.

World Bank. "Global Development Finance", World Bank, Washington, 1997.

World Economic Forum. "The Global Competitiveness Report 1996", Geneva, 1996.

World Trade Organization (WTO). "Annual Report 1996: Trade & Foreign Direct Investment", WTO, Geneva, 1996.

WTO. "Regionalism & the World Trading System", WTO, Geneva, 1995.

ANNEX 1

I. DEFINING FOREIGN DIRECT INVESTMENT (FDI) & RELATED TERMS

Explanation of the terms, as related to Foreign Direct Investment, is provided in this section.

FDI : FDI is an asset that an investor from one country acquires and manages in another country. It is the *"management with control"* of the asset that is significant in FDI and distinguishes the latter from portfolio investments in stocks and bonds etc., in another country (WTO, 1996). Normally, the investors are business firms and the assets they acquire are also firms.

Types of FDI : Three main types of FDI are equity capital (with ownership and control), reinvested earnings and intra-company transactions in the form of borrowing and lending.

> *Equity Capital :* Equity capital is the value of an Multinational Enterprise's (MNE) investment in shares of an enterprise in a foreign country. This category includes mergers and acquisitions and creation of new facilities, often termed "greenfield investments". Equity capital is an important source of FDI for OECD countries.
>
> *Reinvested Earnings* : Reinvested earning is the MNEs share of earning by the affiliate that is not remitted to the parent MNE. The affiliate would normally retain such profit and reinvest it.
>
> *Intra-Company Borrowing and Lending :* This constitutes long and short term borrowing and lending of funds between the MNE and the affiliate.

The three main types of FDIs, as described above, are collected by national statistical agencies and are reflected in the balance of payments statistics by IMF (WTO, 1996). However, comprehensive and comparable data on FDI is yet to be recorded consistently in all countries, which makes conclusions to be drawn from any study on FDI flows difficult.

Flow of FDI : Flows of FDI refer to the movement of investment funds across international borders. This includes outgoing and incoming investment. Investments that do not involve cross-border flows are not counted. Flows of FDI are reported both in *gross and net terms*.

> *Gross Inflow of FDI :* It includes equity and long term debt investments by foreign investors.
>
> *Gross Outflow of FDI :* It includes the repayment of a long term loan and sale of equity to domestic residents.

Net Flow of FDI : It represents the difference between gross inflows and outflows of FDI.

Stock of FDI : It represents the *net* book value of long term capital owned by MNEs in businesses in the host country.

Home Country : The country of the investor or investing firm is termed the home country.

Host country : The country where the assets are acquired or FDI flows in is called the host country.

Parent Firm : The investor firm is known as the parent firm.

Affiliate or Subsidiary : The asset in the host country is called the affiliate.

Multinational Enterprise (MNE) : A multinational enterprise is an organization that engages in the production and distribution of goods and services in two or more nations (Rugman ,1990; Graham & Krugman in Froot, 1993). FDI is, in essence, the creation or expansion of firms that operate across national boundaries *(Graham & Krugman in Froot,1993)*. Direct investment is an integral part of large firms' overall strategy for global production and sales. These firms are the multinational enterprises which serve as the largest sources of FDI and foremost agents of FDI growth in the global economy (McCulloch in Froot, 1993).

(iv) The NAFTA provides for minimum standards of treatment for foreign investors and investments.

(v) The NAFTA provides for full and fair compensation for expropriated investments.

The primary objectives of numbers (iii) and (iv) are to protect Canadian and US investments in Mexico Rugman, 1994).

(c) Target Grandfathering and Negative Lists (Annex 1 and 2 of the NAFTA): The NAFTA replaces the FTA's grandfathering of all existing legislations affecting investments with what has been termed as *target grandfathering* with a series of negative lists. The negative list is in effect a reservation list of all measures and legislations that do not conform with the NAFTA provisions that each signatory party chooses to retain.

TRADE & ECONOMIC POLICY PAPERS

List of Papers on Trade and Economic Policy Issues:

A) TRADE POLICY SERIES

1. Globalization and Public Policy in Canada: In Search of a Paradigm, by Keith H. Christie Document no. 93/01 (January 1993)* SP19A

2. Trade and the Environment: Dialogue of the Deaf or Scope for Cooperation?, by Michael Hart and Sushma Gera. Document no. 92/11 (June 1992) SP18A

3. Globalization: The Impact on the Trade and Investment Dynamic, by Dennis Seebach. Document no. 93/07 (June 1993)* SP25A

4. Merger Control Under Trade Liberalization: Convergence or Cooperation? by Nicolas Dimic. Document no. 93/09 (August 1993)* SP27A

5. Technology Consortia: A Prisoner's Dilemma? by Rhoda Caldwell. Document no. 93/10 (August 1993)* SP28A

6. Optimal Patent Term and Trade: Some Considerations on the Road Ahead by I. Prakash Sharma. Document no. 93/12 (October 1993)* SP30A

7. And the Devil Take the Hindmost: The Emergence of Strategic Trade Policy by I. Prakash Sharma and Keith H. Christie. Document no. 93/14 (December 1993)* SP32A

8. Stacking the Deck: Compliance and Dispute Settlement in International Environmental Agreements by Keith H. Christie. Document no. 93/15 (December 1993)* SP33A

9. Financial Market Integration: The Effects on Trade and the Responses of Trade Policy, by James McCormack. Document nº 94/01 (February 1994)* SP35A

10. The New Jerusalem: Globalization, Trade Liberalization, and Some Implications for Canadian Labour Policy, by Rob Stranks. Document no. 94/02 (February 1994)* SP36A

11. Competition Policy Convergence: The Case of Export Cartels, by William Ehrlich and I. Prakash Sharma. Document no. 94/03 (April 1994)* SP37A

12. The Day After: An Agenda for Diversifying Free Trade, by Keith H. Christie. Document no. 94/04 (January 1994)* SP38A

13. Global Strategies and Foreign Direct Investment: Implications for Trade and the Canadian Economy, by Julie Fujimura. Document no. 94/07 (March 1994)* SP41A

14. Delivering the Goods: Manufacturer-Retailer Relations and The Implications for Competition and Trade Policies, by I. Prakash Sharma and Prue Thomson with Keith Christie. Document no. 94/11 (December 1994)* SP45A

15. North American Free Trade, Subsidies and Countervailing Duties: Issues and Options, par Gilbert Gagné. Document no. 94/13 (July 1994)* SP47A

16. Dangerous Liaisons: The World Trade Organization and the Environmental Agenda, by Anne McCaskill. Document no. 94/14 (June 1994)* SP48A

17. Damned If We Don't: Some Reflections On Antidumping and Competition Policy, by Keith H. Christie. Document no. 94/15 (July 1994)* SP49A

18. Pandora's Box?: Countervailing Duties and the Environment, by Robert T. Stranks. Document no. 94/19 (October 1994)* SP53A

19. Diplomacy at the Leading Edge: Advanced Technology and Canadian Trade Policy, by Gary Luton. Document no. 95/12 (December 1995)* SP70A

20. Capital Controls: Rationale and Implications: For Canadian Trade and Investment Policy, by Ehsan Choudhri and Prakash Sharma. Document no. 96/04 (November 1996) SP77A

21. National Competition Policy Philosophies in the Triad: Considerations for Trade Policy, by Philip B. Marsden and I. Prakash Sharma. Document no. 96/06 (September 1996)* SP79A

22. Canada: Drawers of Water, Hewers of Wood and Dangers of Other Myths, by Prakash Sharma, Allen Brown, and David Weiner. Document no. 96/07 (December 1996)* SP80A

B) TRADE DEVELOPMENT SERIES

1. From a Trading Nation to a Nation of Traders: Towards a Second Century of Trade Development, by Andrew Griffith. Document no. 92/05 (March 1992)* SP12A

2. Exports and Job Creation, by Morley Martin. Document no. 93/06 (June 1993)* SP24A

3. The Impact of Exports: An Input-Output Analysis of Canadian Trade, by James McCormack. Document no. 94/24 (December 1994)* SP58A

C) REGIONAL TRADE AND ECONOMIC SERIES

1. Different Strokes: Regionalism and Canada's Economic Diplomacy, by Keith H. Christie. Document no. 93/08 (May 1993)* SP26A

2. Japan Trading Corp.: Getting the Fundamentals Right by I. Prakash Sharma. Document no. 93/16 (December 1993)* SP34A

3. Canada in the Americas: New Opportunities and Challenges, by Conrad Sheck, Colin Robertson, Jamal Khokhar, Nicolas Dimic, and Keith Christie. Document no. 94/06 (April 1994)* SP40A

4. China 2000: The Nature of Growth and Canada's Economic Interests, by Steve Lavergne. Document no. 94/10 (May 1994)* SP44A

5. The Japanese Way: The Relationship Between Financial Institutions and Non-Financial Firms, by James McCormack. Document no. 94/16 (July 1994)* SP50A

6. Towards Regional Economic Blocs: Are We There Yet?, by Julie Fujimura. Document no. 95/01 (February 1995)* SP59A

7. Changing Partners: Trends in Canada's Regional Economic Relations, by Steve Wilson. Document no. 95/02 (March 1995)* SP60A

8. Fact or Fancy?: North Asia Economic Integration, by Steve Lavergne. Document no. 95/03 (March 1995)* SP61A

9. With or Without You; Argentina, Brazil & NAFTA, by Stephen Wilson. Document no. 95/09 (August 1995)* SP67A

10. The Four Amigos and Beyond: Towards the Free Trade Area of the Americas, by Keith Christie. Document no. 95/10 (October 1995)* SP68A

11. Changes in the Neighbourhood: Reflections on Mexico in Transition, by Thomas Legler. Document no. 96/02 (February 1996)* SP75A

12. Why We Were Right and They Were Wrong: An Evaluation of Chapter 19 of the FTA and NAFTA, by Ann Penner. Document no. 96/05 (September 1996)* SP78A

13. European Monetary Union and its Implications for Canada, By Robert Hannah. Document no. 97/01 (March 1997)* SP81A

D) OTHER ECONOMIC PAPERS

1. World Population Growth and Population Movements: Policy Implications for Canada, by Michael Shenstone. Document no. 92/07 (April 1992)* SP14A

2. For Effective and Appropriate Sanctions, par Jean Prévost. Document no. 93/04 (March 1993)* SP22A

3. Black Gold: Developments in the World Oil Market and the Implications for Canada, by Sushma Gera. Document no. 93/05 (February 1993)* SP23A

4. Determinants of Economic Growth in Developing Countries: Evidence and Canadian Policy Implications, by Rick Mueller. Document no. 94/08 (April 1994)* SP42A

5. Still an Albatross? The LDC Debt Crisis Revisited, by Rick Mueller. Document no. 94/09 (May 1994)* SP43A

6. Pro-Active Sanctions: A New/Old Approach to Non-Violent Measures, by Dr. Nicholas Tracy. Document no. 94/17 (June 1994)* SP51A

7. A View of the Forest: Environmental Stress, Violent Conflict, and National Security, by Rob Stranks. Document no. 95/05 (April 1995)* SP63A

8. The Geographic Distribution of Canada's Bilateral Assistance: Alternative Approach, by Nicolas Dimic. Document no. 95/11 (August 1995) SP69A

9. Dealing with Diversity: Canada's Economic Relations with Developing Countries, by Keith Christie and David Preston. Document no. 95/15 (December 1995)* SP73A

10. China: Environmental Stress and National Security, by Rob T. Stranks and Nicolino Strizzi. Document no. 96/01 (February 1996)* SP74A

11. "New" Growth Theory and Development Assistance, by James P. Walker. Document no. 96/03 (April 1996)* SP76A

TRADE & ECONOMIC POLICY COMMENTARIES

No. 1 The Uruguay Round: What's In It For The Developing Countries, by Robert T. Stranks * (March 1994).

No. 2 Outward Direct Investment: Implications for Domestic Employment, by Robert T. Stranks and Julie Fujimura* (April 1994).

No. 3 Trade and Direct Investment Statistics: The Twain Have Met, by James McCormack * (May 1994).

No. 4 Economic Sanctions: Foreign Policy Foil or Folly?, by Robert T. Stranks * (May 1994).

No. 5 Recent Capital Flows to Latin America: Too Good to Last?, by Richard E. Mueller * (August 1994).

No. 6 Not Out of the (Bretton) Woods Yet: Exchange Rate Disequilibria, Trade and Suggested Reforms, by James McCormack* (February 1995).

No. 7 Takin' Care of Business: The Impact of Deficit Reduction on the Trade Sector, by James McCormack* (March 1995).

No. 8 The Trouble with Numbers: Military Spending in Developing Countries, by James McCormack* (June 1995).

No. 9 Unfinished Business: Towards a Global Environmental Organization, by Rob Stranks* (July 1995).

No. 10 Alternative Financing for the United Nations: An Idea Whose Time Has Finally Come?, by James P. Walker* (December 1995).

No. 11 Traders in Tennis Shoes: Derivatives, Volatility, Risk and Supervisory Issues, by James McCormack* (May 1995).

No. 12 Prospects of Further Reforms in India, by I. Prakash Sharma* (December 1995).

No. 13 Restructuring Japan's Financial System: Looking Beyond the Storm, by Julie K. Fujimura* (February 1996).

No. 14 Look Before you Leap: "Core" Labour Rights, by Robert T. Stranks* (April 1996).

No. 15 Trade in the '90s: An Overview of Canada's Performance, by Julie K. Fujimura* (June 1996).

No. 17 Environmental Refugees?, by Robert T. Stranks* (January 1997).

No. 18 The Right Tool for the Job? Child Labour and Trade Sanctions, by Robert T. Stranks* (June 1997).

No. 19 APEC and FEEP: An Evolving Integrated Assessment, by Robert T. Stranks with Ravish Mitra* (November 1997).

No. 20 Developments in Canada's Trade and Foreign Investment in 1997*, by Anjali Bedi, Shenjie Chen, Clea Coronel, Suzanne Desjardins, with Prakash Sharma (March 98).

Also Available:

EET Reference Documents

No. 1 International Trade Policy Research Survey, by Colleen Hamilton *
(May 1997).

No. 2 Trends in FDI: A Comparison of Canada with the USA & Mexico*,
by Nipa Banerjee, (November 1997).

No. 3 Market Access and Environmental Protection: A Negotiator's Point of View*,
by Andrew Griffith (October 1997).

No. 4 International Trade Theory and Policy Bibliography*, by Nipa Banerjee
(November 1997)

* **available in french/disponible en français**